Zurich Investments

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An update to the Investment Outlook 2016

A Message to Investors

Despite economic uncertainties, relative value still favours equities

September 2016

Dear Investor,

We firmly believe that active asset allocation is unavoidable and can provide significant benefits to investors. Following the recently issued update to our Investment Outlook, we have implemented some significant changes in our asset weightings.

We have increased the equity allocation across our multi-asset funds, including our Pathway range, the Active Asset Allocation Fund, and our long-standing Balanced, Performance and Dynamic funds.

The rationale for the equity move is threefold. First, the dominant US stock market, which has been in a trading range for the last 18 months, has recently broken out on the upside. This is a strong technical factor and may result in further gains in the S&P 500 Index over the coming months. Secondly, equities remain attractively valued on a relative basis versus bonds and cash, despite the fact that the US P/E multiple is above its historical norm. Lastly, sentiment is quite hesitant as it has been for some time now. Strong equity performance can often result when investors face such a 'wall of worry'.

Our Bond allocation has decreased as percentage of our funds and the duration (which indicates the sensitivity of a bond price to interest rate changes) has also been reduced, as we feel currently that bonds offer little long term value.

As we come towards the end of the third quarter of 2016, we maintain one of the key assertions made over the past couple of years: that volatility will be a feature of markets, but most importantly, will continue to provide opportunities to active managers.

Finally, despite the turbulent investment environment we are pleased to tell you that all our in-house multi-asset funds are in positive territory for the year, with the team having successfully navigated the markets. The importance of this cannot be understated. At a time when interest rates remain at an all-time low there are fewer and fewer savings options available. Being able to consistently offer investors a positive, inflation beating performance is of great benefit.

Richard Temperley

Richard Temperley
Head of Investment Development

Volatility to continue to provide opportunities

Since our last investment outlook in January, equity markets have been subjected to increased volatility due to a confluence of events. These include economic growth concerns in China, severe oscillation in the price of oil, negative interest rates in some regions and, more latterly, Brexit. Investors are also focussed on the US interest rate cycle and the likely timing of the next rate rise.

Economic uncertainty has resulted in many equity markets struggling in the first half of the year; although the US and UK markets have been notably resilient in local currency terms. Despite volatility global equity returns to euro based investors have been positive year-to-date. Equities remain attractively valued compared to bonds and cash.

Long-term eurozone bond yields reached fresh all-time lows towards the end of June. Despite the lack of value, bonds have been supported by the tailwind of aggressive ECB monetary policy action.

Global growth expectations have been reduced

- Global growth is likely to have slowed down from 2015 levels.
- Monetary policy is still accommodative globally and indeed a number of central banks are likely to continue to ease policy further.
- UK growth is likely to be negatively affected by Brexit.
- Economic growth in the eurozone could be held back by contagion effects following the UK referendum result.

Upside risks to outlook

- Global growth bounces, buoyed by central bank action.
- Commodity prices continue to rise, allaying deflationary fears and supporting many emerging markets.
- Further supportive monetary policies in Europe and Asia.
- Further interest rate increases in the US are interpreted as a vote of confidence in the economy and a welcome return to normality.
- Additional fiscal expansion to stimulate growth.

Downside risks to outlook

- Economic growth slows in the Eurozone due to Brexit contagion.
- Policy tightens in the US; how will markets react?
- Political and structural risks in Europe increase; polarisation in US politics.
- Further Chinese devaluation of the yuan would be a further drag on growth and inflation in the rest of the world.
- Geo-political risks remain with the ISIS conflict and the migration crisis in Europe.

“Economic growth in the eurozone could be held back by contagion effects following the UK referendum result.”

Equities are still the more attractive asset class on relative valuation grounds

- Equity markets remain attractively valued versus cash and bonds but have become more expensive on a price/ earnings multiple basis.
- Consensus expectations for earnings growth in 2016 have now dropped to c.2.1% from c.7.6% at the beginning of the year.
- The US equity market has broken out to the upside;further gains are possible as cash on the sidelines enters the market.
- Structural issues remain the backdrop in Europe; Asia's underperformance seems to have ceased and its markets are starting to look more attractive now.
- The dividend yield on pan-European equities at 3.6% offers an income uplift compared to existing corporate and government yields.

Ultra-low bond yields – an attractive long-term investment?

- ECB policy rates should remain low for an extended period of time. Subdued economic growth and low inflation are the main reasons for this.
- Valuations, however, are not supportive of fixed income as a long-term investment. Further gains in bonds prices so far in 2016 have been mainly due to quantitative easing by the ECB. Yields could begin to pick up slightly in the second half of the year.
- There is some expectation that the US central bank will raise interest rates this year. However recent experience has demonstrated that when the central bank has any concerns at all about the US economy or global financial conditions they will err on the side of raising rates later than the market expects.
- Global inflation, while remaining low by historical levels, may see a slight pick-up due to rising commodity prices and some upside wage pressures.

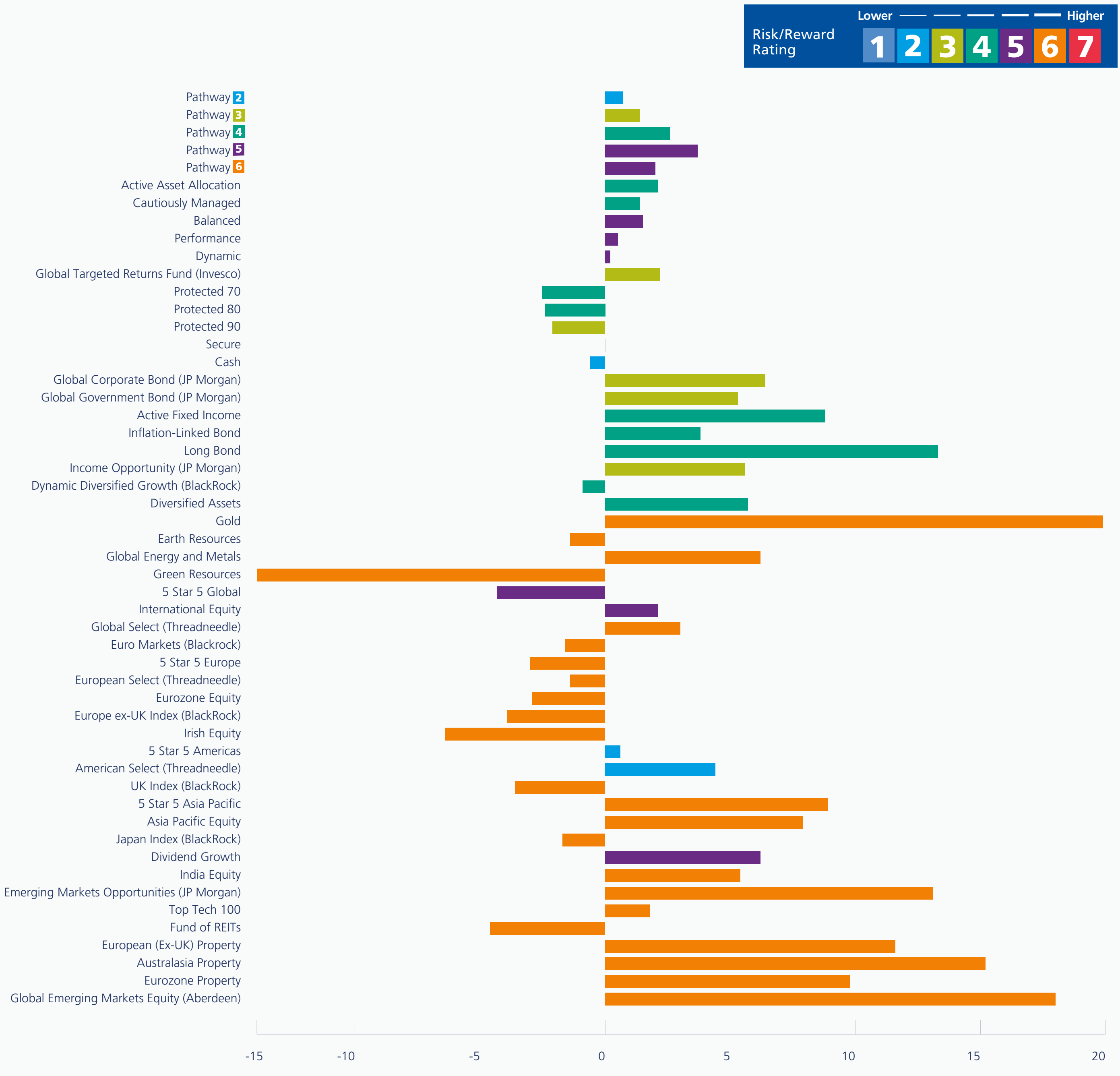
Low intensity currency war continues

- No major country has the inflation justification for actively pursuing a stronger currency.
- Currency weakness remains a preference for the eurozone as the current ECB's monetary policy is no longer effective.
- Japan's preference for a weaker currency is offset by its strong external position and the limits of the global 'zero sum game' of currency manipulation.
- The US dollar's relative strength reflects the comparative strength of its economy plus the actual and potential interest rate support compared to 'zero rate' currencies.

> "There is some expectation that the US central bank will raise interest rates this year. However recent experience has demonstrated that when the central bank has any concerns at all about the US economy or global financial conditions they will err on the side of raising rates later than the market expects."

Performance to 31 August 2016

The benefits of diversification



Annual management charges (AMC) apply. The fund returns shown are net of the AMC deducted by each provider in their unit prices. This will vary for each provider, and any difference will impact the relative performance of the funds shown. The fund returns are based on an investment in the funds and do not represent the returns achieved by individual policies linked to the funds. These fund returns may be before the full AMC is applied to a policy. The actual returns on policies linked to the specified fund will be lower because of the effects of charges and in some cases a higher management charge.

Source: Financial Express as at 01/09/2016

Warning: Past performance is not a reliable guide to future performance.
Warning: The value of your investment may go down as well as up.
Warning: Benefits may be affected by changes in currency exchange rates.
Warning: If you invest in this product you may lose some or all of the money you invest.

An active approach to investing money

At Zurich we aim to deliver long-term consistent investment performance.

We believe that people need people to look after their money so we take a 'hands-on', active approach to selecting the right assets and the right stocks to fit investment portfolios.

Financial markets will always give opportunities to good active managers to deliver better performance so we position ourselves to capture that.

Our investment team, based in Blackrock, Co. Dublin, is responsible for funds under management of approximately €19.5 billion, of which pension assets amount to €9.1 billion.

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*Source: Zurich Life, 30 June 2016

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For more information, visit the fund section at **zurichlife.ie**

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